

## FUND BALANCE

### Fund Balance Recommendation for FY2015 Budget

We are recommending the City utilize \$400,000 of Fund Balance to support the FY2015 budget. This is the same level of Fund Balance approved as part of the FY2014 budget. Over the past three years, the City has reduced its budgeted use of Fund Balance by almost 50% from its high of \$765,000 in the FY2011 budget, when exceptional economic conditions warranted the increased use of Fund Balance to mitigate negative effects to the tax rate.

We estimate that the City will end FY2014 with an Unassigned Fund Balance of just over \$3.6 million, which would represent 10.6% (over 37 days' worth) of anticipated FY2015 operating expenses of \$35,100,000. Using \$400,000 of Fund Balance in FY15 could drop this to 9.2% (34 days' worth) of operating expenses. However, as appears will be the case in FY14, we anticipate being successful in FY15 at taking in slightly more revenues and expending less than budgeted, such that we will end the year using little or no Fund Balance and possibly even adding to its overall balance.

As always, it is important to note that utilizing Fund Balance to support general operating expenses on a recurring basis is not sustainable. We are pleased that the City Council recognizes this and has scaled back the use of fund balance over the past several years to ensure the City budget is structurally balanced.

### What is Fund Balance?

Fund Balance is a key measurement of the accumulation of all expenses and revenues since the municipal government's creation. It is not excess cash, although it is partially comprised of cash and investments. We might compare Fund Balance of a municipality to that of owner's equity in a private company. In the banking industry, oversight regulators focus in on "equity" as a key to the fiscal health of an institution. Minimum standards are established and monitored. It is not much different with the City of Brewer's Fund Balance.

Portions of Fund Balance called "*Non-Spendable*", "*Restricted*", and "*Assigned*" represent funds the Council has designated for some future spending purpose.

"*Unassigned Fund Balance*" is the contingent fund maintained for many purposes. Some call this "surplus", but that term can be mis-construed by taxpayers as "*spendable without significant consequences*". Reviewing the unassigned portion of Fund Balance

is, in essence, a focus on assuring long-term solvency—certainly an essential component of the entire City budgeting process.

## **What Role Does Fund Balance Play in a City's Finances?**

An important goal of a local government is to maintain a stable tax and revenue structure while providing the orderly delivery of desired and necessary services to residents. Fund Balance plays a key role in that stability. Achieving and maintaining a healthy Fund Balance gives the City of Brewer a strong fiscal foundation that allows it to respond to differing needs of the community. Depending on the size of the Fund Balance, this account can be drawn upon to respond to City Council directives such as the following:

- Provide working capital (cash) to avoid constant short-term borrowing
- Maintain the stability of its tax rate through occasional draw downs and, alternately, absorbing temporary excess revenues in good years
- Maintain or improve the City's credit standing
- Provide a fallback for any temporary economic uncertainty in tax growth
- Provide for unforeseen major capital or mandatory expenditures
- Allow absorption of large hits, such as abatements or lawsuits, without negatively impacting the tax rate in a particular year
- Fund initial expenditures of planned capital projects that have yet to be bonded
- Provide working capital for unexpected increases in uncollected taxes

Maintaining a proper minimum Fund Balance also provides evidence to the City's bondholders and bond rating agencies of the City's continuing financial stability and credit worthiness. In the financial marketplace, a sound Fund Balance and Fund Balance policy are credit strengths that result in lower borrowing costs for the city.

## **What Represents a "Healthy" Fund Balance?**

Fund Balance needs vary from community to community and depend on a number of factors, including the type and stability of revenues, the size and structure of the debt load, and the nature of expenditures. Before GASB Statement No. 34 changed fund balance to calculate it net of all liabilities, Unassigned Fund Balance for a municipality typically ranged from 5 to 15% of total operating expenses, with 8.3% (one month's operating expenses) being the typical minimum target.

Given the economic turmoil and uncertainty the country has been facing, industry experts have increased the recommended fund balance to as much as two months worth of operating expenses or higher depending on the community's particular situation. The City needs a healthy Fund Balance to be able to maintain its ability to respond to other unforeseen circumstances that may arise.

Another way to analyze the health of the Fund Balance looks at total Fund Balance as a percent of gross revenues. Bond rating agencies use this as one measure to determine the risk level of our bonds.

The chart below shows Brewer's actual Fund Balance for the last five fiscal years and projected Fund Balance for the current fiscal year.

**City of Brewer  
Fund Balance History and Ratios**

**Fiscal Years 2009 to 2014**

(000s)

	Fiscal Year Ending					
	6/30/09	6/30/10	6/30/11	6/30/12	6/30/13	6/30/14
<b>FUND BALANCE</b>						(estimated)
<b>Unassigned</b>	\$3,817	\$3,634	\$3,407	\$3,643	\$3,463	\$3,625
<b>Non-spendable,restricted,committed</b>	\$1,964	\$1,989	\$2,559	\$2,194	\$1,312	\$1,323
<b>TOTAL FUND BALANCE</b>	\$5,781	\$5,623	\$5,966	\$5,837	\$4,775	\$4,948
 <b>Operating Expenditures</b>	 \$31,695	 \$33,836	 \$33,193	 \$33,892	 \$33,466	 \$35,100
<b>Gross Revenues</b>	\$31,602	\$33,660	\$33,536	\$33,763	\$32,554	\$35,100
 <b>Unassgn. Fund Balance as % of Op. Exp.</b>	 12.0%	 10.7%	 10.3%	 10.7%	 10.3%	 10.3%
<b>Total Fund Balance as % of Gross Rev.</b>	18.3%	16.7%	17.8%	17.3%	14.7%	14.1%

**How Should the City of Brewer Approach Setting Its Fund Balance Level?**

This is a matter of examining all the objectives recommended by the City management staff to establish funding for known goals and to maintain fiscal health. Additionally, the City Council, as the legislative body, must perceive where the taxpayers wish to set their priorities for the greater good of the City. Then, the City Council must establish the delicate balance between short-term and long-term objectives. From this, we establish a target for fund balance for that year and prudent management says that it should be reviewed annually at budget time. Based upon changing conditions that target should be flexible in either its dollar amount or its percent in relation to total operating expenses.